UNITED STATES POSTAL SERVICE®

TESTIMONY OF
JOHN E. POTTER, POSTMASTER GENERAL/CEO,
BEFORE A JOINT HEARING OF THE
COMMITTEE ON GOVERNMENT REFORM,
UNITED STATES HOUSE OF REPRESENTATIVES,
AND THE
COMMITTEE ON GOVERNMENTAL AFFAIRS,
UNITED STATES SENATE

MARCH 23, 2004

Good afternoon, Chairman Davis, Chairman Collins and Committee members. I am pleased to be with you today as we continue the critical discussion about the need for comprehensive reform of the legislative framework governing the Postal Service.

In the months since the President's Commission on the United States Postal Service issued its final report endorsing the very real need for postal legislative reform, virtually every stakeholder has taken an active part in this conversation.

As we have learned through the course of multiple hearings held by both Committees, there is a broad consensus in support of postal reform. There is a common understanding that the mail is today – and will remain for many years to come – a key part of the nation's communication system. There is a common understanding that the mail is the foundation of a vital industry that is a large and important contributor to the nation's economy. In short, there is a common understanding that deliberate and measured action must be taken to protect the right of everyone in America – no matter who, no matter where – to affordable, universal postal service.

Without needed change, mail may cease to be affordable. Without affordability, what our nation takes for granted as universal service – six-day delivery to virtually every address in America – will be in jeopardy.

Within that context, we have the opportunity and the obligation to develop the right solutions to the challenges facing the nation's mail system so that every family and every business in America continues to enjoy – and benefit from – affordable, universal mail service.

The nation's elected leaders rose to a similar challenge more than three decades ago when they enacted the Postal Reorganization Act of 1970. The business model they created – which was the right model for its time – was effective. As a result, the Postal Service is self-sufficient. Postage rates have largely tracked the rate of inflation. And, by the end of this fiscal year, we will have achieved the Act's mandate that the Postal Service "break even" over time.

However, in the course of only a few short years, we have seen the assumptions of that 34-year old business model rendered obsolete. That model relied on continuing mail volume growth to generate the revenue necessary to fund the costs of expanding our network to meet the needs of a growing nation. This is no longer the case.

Mail volume has declined in each of the last three years, dropping more than five billion pieces from its peak in 2000, representing $4.5 billion less in revenue. During the same three-year period, the number of addresses we served increased by 5.4 million. This combination of factors – declining mail volume contrasted with the costs of a still-growing service network, resulted in a net loss in three of the last four years.

An analysis of volume trends also reveals fundamental shifts in the mail mix. In 2003, reflecting an ongoing trend, First-Class Mail was less than half of total volume. The impact of technological advances, especially on First-Class Mail, demonstrates that profound structural changes in how consumers and businesses communicate are at work. Electronic communications are increasingly being used for transactions that, in the past, have almost universally taken place through the mail.

The robust growth of private-sector services delivering packages and time-sensitive communications has also altered the competitive landscape. These factors will contribute to a diminished rate of mail volume growth and, perhaps, an absolute decline in volume, even as the delivery infrastructure, and its associated costs, continues to expand.

First-Class Mail has been, historically, the greatest supporter of our universal delivery network. It has also experienced the most significant volume erosion, declining by more than 3 billion pieces from 2002 to 2003. While Standard Mail volume grew by 3 billion pieces over the same period, its overhead contribution is only one-third that of First-Class Mail. Standard Mail would have to grow at three times its present rate to balance the loss of First-Class Mail. That level of growth is unlikely. In 2003, we experienced modest growth in package services, but total package volume, at 1.1 billion pieces, is only one percent of First-Class volume. No other class – or combination of mail classes – can produce the volume growth necessary to offset the decline in First-Class overhead contribution. This has placed extreme pressure on our bottom line.

As we proceed with consideration of reform, we must be clear that our goal is preserving and protecting a *national* postal system. And that system is far more than simply the organization called the Postal Service. It is also composed of commercial mailers, nonprofit mailers, industry organizations, consumers, suppliers, current and former Postal Service employees, the organizations that represent them, and everyone else with a stake in the continuation of this vital, national service.

During this critical conversation, we have heard from many of them. Some have suggested that the Postal Service should not have authority to pursue innovative pricing practices widely used in the private sector. Some have suggested that our long and successful history of worksharing, which has held down our costs and contributed to substantial mail volume and industry growth, should be ended. Some have suggested that that the Postal Service operate within the limits of a price cap, but without the necessary level of flexibility to manage significant elements of our costs. Some have suggested that our ability to compete be limited by our withdrawal from certain product categories.

Despite the differing purposes and priorities of these groups, each has one thing in common – reliance on a postal system that meets the special needs of each while serving the common needs of all – affordable, accessible, universal mail service. To assure this outcome, each must be engaged and prepared to be a part of the process of change. We cannot succeed if any one expects only the others to be affected. Nothing can be off limits.

I recognize, too, that as we collectively explore the options available to us, the Postal Service also has the obligation to demonstrate that it is managing its business as effectively as possible.

That is what we are doing. Since I assumed the role of Postmaster General, transformation of the Postal Service has been our central focus. And I am pleased that the President's Commission on the Postal Service acknowledges that our Transformation Plan is guiding us to substantial progress in adapting to an uncertain future. Clearly, it is taking us in the right direction as we improve operational efficiency, add value to our products and services, and enhance a performance-based culture.

While the Transformation Plan became our organizational vision in 2002, the ongoing process of transformation began before then through our breakthrough productivity initiative. The year 2000 marked the first of a record four straight years of increases in total factor productivity.

Even without the effect of our change in payments to the Civil Service Retirement System, we have delivered $5 billion in cost savings since 2000. This includes $2.7 billion in savings resulting from Transformation Plan initiatives over the past two years. We are on track to surpass the $5 billion in savings called for by the Transformation Plan over the five-year period ending in 2006.

We are closely examining other opportunities for cost savings, as well. The continuing decline in single-piece, First-Class Mail, combined with the advances we have made in our automated mail-processing environment will provide opportunities for changes to our distribution and transportation network.

We have reduced our career employee complement by more than 85,000 – a reduction of more than ten percent from its peak level in 1999. That is a reduction of an additional 15,000 positions since I testified before the Governmental Affairs Committee in November and 5,000 positions since my appearance before the Special Panel on Postal Reform and Oversight in January. Fewer than 70 American companies have as many as 85,000 employees on their rolls.

Consistent with our Transformation Plan goal of enhancing a performance-based culture, we have established pay-for-performance systems for managers, executives, postmasters and supervisors. The new system links 100 percent of all pay increases to performance. We have improved the workplace environment, measured both by reductions in grievances awaiting arbitration and quarterly employee surveys.

We have brought service performance and customer satisfaction to the highest levels in our history. We are aggressively managing the business. This will not change.

In addition to the Transformation Plan strategies that have contributed to these successes, the recent legislation adjusting the Postal Service's payments to the Civil Service Retirement System helped us achieve a welcome and needed level of financial stability.

In 2003, extremely focused efforts in managing our business and the impact of the Postal Civil Service Retirement System reform legislation, combined to result in a net income of $3.9 billion. Even without the welcome relief of the CSRS legislation, continued cost reductions and increased productivity would have resulted in a net income of $900 million – a fifty percent increase over plan.

We are particularly grateful for the understanding and cooperation of Chairman Collins, Chairman Davis, members of Committees represented here today, as well as the Administration and the General Accounting Office for their prompt action in addressing Postal Service retirement obligations.

By partially correcting Postal Service CSRS funding requirements, the legislation will allow us to hold rates steady until 2006. It has contributed to our ability to reduce outstanding debt by more than one third – from $11.1 billion to $7.3 billion – in fiscal year 2003. It will help us reduce debt even more this fiscal year.

This same legislation, however, creates new financial obligations that increase costs and place unnecessary upward pressure on rates, but provide no direct benefit for ratepayers and users of the mail. And, because these costs have a long-term future impact on our financial situation, we strongly believe they must be addressed immediately.

First, as I have stated previously, the Postal Service should not be responsible for funding CSRS retirement benefits earned by postal employees while they served in the military. This $27 billion obligation, $17 billion of which represents a retroactive charge to 1971 and which has already been paid to retirees, should be returned to the Treasury. Military retirement costs have no connection to the operation of the Postal Service or the services it provides. The nation as a whole benefited from the periods of military service involved – most of which predated the creation of the Postal Service – and, as such, the associated costs should not be borne by postal ratepayers. The President's Commission shares our view on this matter.

Second, the Postal Service proposes the elimination of the escrow account requirement established by the CSRS legislation. This provision requires that, after 2005, the "savings" resulting from the legislation be placed into an escrow account pending Congressional authorization for their use. The "savings" represent the difference between the Postal Service's new CSRS payment schedule and the old. The simple fact is that, under present postage rates, there will be no funds available after 2005 to place in the escrow account. While we will be paying less for our CSRS obligations, by 2006 any "savings" will have been consumed by inflationary cost increases for employee compensation, benefit expenses for active and retired employees, and for supplies and services associated with serving an expanding delivery network.

The escrow account will be funded by postal ratepayers through higher postage rates. That is because it will be necessary to raise rates in 2006 beyond what would be required simply to offset inflation. We estimate that the escrow requirement, by itself, will result in a 5.4 percent rate increase. This could mean that the average rate increase sought for 2006 could be in the double digits.

Given the continuing diversion of high-contribution First-Class Mail to other channels of communication, maintaining the escrow requirement could accelerate this diversion, exacerbating the problems legislative reform is intended to address.

As I said, the Postal Service strongly urges the elimination of the escrow requirement and the enactment of our preferred proposal. If enacted and the military retirement funding requirement is transferred back to the Treasury, the Postal Service would have fully funded and, in fact, over-funded our CSRS payment obligation. We would then be in a financial position to pre-fund post-retirement health benefit obligations on a current basis.

In previous appearances before both the Committee on Governmental Affairs and the Special Panel on Postal Reform and Oversight, I have discussed specific recommendations made by the President's Commission on the Postal Service in its final report. I have also expressed my support of the five key principles that the President urged Congress to consider in enacting postal reform legislation. I will briefly review the Postal Service's position on each of these issues.

We agree that the Postal Service should take advantage of corporate best practices. We will continue our pursuit of private-sector strategic partnerships where they help us enhance efficiency, reduce costs or improve service. We will continue to work with the mailing industry to expand worksharing to encourage the use of the mail and contribute to more efficient operations for the Postal Service.

We will continue more innovative approaches to how we buy products and services – including the revision of our purchasing regulations – to reflect corporate best practices such as supply-chain management. Our success in this effort will depend largely on our ability to leverage our size to obtain the best value for every dollar spent on supplies and services. We can maximize cost savings in our buying activities only if every purchasing decision is driven by best value. Our ratepayers deserve nothing less.

We agree with the principle of transparency. While the President's Commission noted that, in many respects, our reporting often exceeds what is required of Federal agencies, we are enhancing financial reporting in a number of key areas. These include annual and quarterly financial reports and enhanced disclosure and reporting of significant events reflecting SEC-type reporting requirements of publicly traded companies.

We agree with the principle of flexibility. In short, management must have the flexibility to manage by having the authority to reduce costs, set rates, and adjust its business to meet its obligations to customers in a dynamic marketplace. I consider this the litmus test of postal reform.

In certain key areas – the determination of funds needed to operate the system and adjustments to our retail and processing network to meet changing conditions – the Commission has proposed that other bodies, either the proposed Postal Regulatory Board or a new Postal Network Optimization Commission, assume these responsibilities. This distances the operators – those with the day-to-day responsibility of running the postal system – from key decisions, reducing rather than increasing management flexibility.

We agree with the principle of a self-supporting Postal Service. A reformed pricing regime can help produce this result by providing the flexibility to respond to market needs while covering costs.

A self-supporting Postal Service would also include our ability to retain earnings, a concept called for in our Transformation Plan and endorsed by the President's Commission. This would provide a revenue stream that could finance capital expenditures and "smooth out" business cycle impacts on overall financial performance.

I have pointed out that declines in mail volume and changes in the mail mix present us with an extremely challenging revenue outlook. With that in mind, we are continuing to identify and pursue growth opportunities. As we face an uncertain future, the Commission's recommendation restricting Postal Service activities primarily to those offered today could prove to be unnecessarily limiting to future revenue opportunities that would protect our ability to provide universal service.

We agree with the President's fifth reform principle of accountability. With increased management flexibility, there must be an appropriate level of independent oversight to protect the interests of all mail users. Yet the Commission's proposed Postal Regulatory Board would have the authority to revisit the letter and mailbox monopolies and universal service. From our perspective, these are broad public policy issues – not regulatory issues. There should be standards drawing a clear line between what is appropriately a managerial function within the oversight of the Governors or Directors, what is a regulatory function committed to the regulator, and what is a public policy function reserved to the nation's lawmakers. Of course, accountability must also be a part of every Postal Service activity, as well.

To the President's list of five guiding principles for reform, I would add a sixth: a commitment to the collective-bargaining process. The give and take of the process assures that interests of our employees and our customers are considered within the larger picture of the Postal Service's financial situation. We agree with the Commission that a more efficient process can benefit all parties and that the addition of a mandatory mediation step – if negotiations have not resulted in a new agreement – could help forge a final resolution or limit the issues that must be addressed if interest arbitration becomes necessary.

The President's principles for reform provide an important framework that can guide the development of an effective new business model for the Postal Service. And, as we work within the constraints of today's model, we are taking every opportunity to drive growth by adding value to our products and services.

In the area of rates, we have developed an innovative negotiated service agreement with one of our largest mailers. By reducing costs for the Postal Service and the mailer, the agreement allows us to offer rates that encourage increased First-Class Mail volume. Early results indicate that this approach is successful and we are working with other mailers on similar agreements.

To increase the use of our traditional products, we are using technology to add value to the mail through the development of new features and services. Our Confirm service – one of the first of our Intelligent Mail initiatives – provides the Postal Service and mailers with a rich stream of information about mail as it moves through our system. It helps the Postal Service improve processing efficiency and helps mailers better achieve their business objectives.

For the Postal Service, the concept of retail is no longer simply the four walls of the Post Office. Our popular website, www.usps.com, lets customers purchase postage, obtain mailing information, change their address, have their mail held, create and print address labels with or without postage, request free carrier pick up of prepaid packages on the next business day, get information about the delivery of their packages, and create and mail greeting cards. USPS.com brings the Post Office right to millions of American homes and businesses, making the use of our products and services quicker, easier and more convenient than ever.

We have developed creative new products that help mailers make their message stand out from the rest. We have made it easier for customers to return merchandise. And, through strategic partnerships with other delivery firms, we are taking better advantage of one of our core strengths – the “last mile” of the delivery process.

Clearly, with service performance at an all time high, with customer satisfaction at record levels, with innovative products and services, and with an expanded period of rate stability, mail today offers better value than at any other time. We will stay focused on enhancing the value and relevancy of mail.

Yet we are faced with structural issues of such magnitude that, if left uncorrected, will transcend market opportunities, exhaust our ability to reduce costs, and, frankly, require us to think about the unthinkable: how long can we afford the cost of universal service as we know it today?

Despite our success in cutting costs over the last four years, this very success in this area restricts future opportunities for cost control. We have aggressively managed costs and managed the servicing of our expanding delivery network. As our costs continue to rise, we must recognize that a significant portion of Postal Service costs originates with requirements imposed on us by legislation. If reform is to succeed, these cost issues must be addressed. That is why future legislation has to provide flexibility in this area.

For example, International Mail is an area in which we have been given greater freedom over pricing and products. But there are greater restrictions on international air transportation. This is because the Department of Transportation determines the rates we must pay airlines. The Postal Service cannot negotiate directly with carriers for international air transportation costs as we can – and do – for domestic mail, which has allowed us to remove significant domestic transportation costs.

This lack of flexibility in international transportation is a significant cost barrier. Our annual costs in this area are nearly $200 million per year. Market-based pricing could reduce that by more than half, to less than $100 million. Change in this model would reduce Postal Service costs and, perhaps, international rates. By being able to offer market-based rates in this highly competitive area, we would have an exceptional opportunity to increase mail volume by providing more affordable options for our mailers.

There are also savings opportunities connected with appeal procedures available to our union-represented employees. Today, these employees may select a number of different dispute-resolution procedures for the same issue. These include the contractual grievance-arbitration procedure and the Equal Employment Opportunity appeals process. These two forums can produce conflicting resolutions and, in some cases, resolutions that are at odds with equity issues established through collective bargaining. The collective-bargaining process should result in labor agreements that allow the parties to resolve workplace disputes through processes they have created and which they control.

We strongly believe that a single appeal process – one that is the product of agreement between the parties – can protect the rights and interests of employees, their representatives and the Postal Service.

By far, the largest single category of costs beyond our span of control is employee benefits. More than 70 percent of Postal Service costs are personnel-related. And benefits constitute more than 25 percent of personnel costs. We have proposed that the collective bargaining process, which covers almost 90 percent of our career workforce, be expanded to include the negotiation of benefits in addition to wages, hours and conditions of employment. In short, everything should be on the table. Some of the key benefit programs enjoyed by our employees, because they are mandated by statute, are currently beyond the scope of collective bargaining.

In 2003 alone, nonnegotiable benefit costs, including retirement contributions, health benefits, life insurance, retiree health benefits and workers' compensation represented more than $13 billion – twenty percent of our operating expenses. These costs continue to increase year to year at rates exceeding normal inflation. While the Postal Service negotiates the employer share of health benefit premium payments with its unions, the actual premium costs and benefits offered by the plan are established by the Office of Personnel Management. The workers' compensation program available to our employees was established by statute and is administered by the Department of Labor. Similarly, annuity payments and health benefits for Postal Service retirees are established by law, not by collective bargaining.

Benefit costs have grown from $7.9 billion in 1990 to $16.1 billion in 2002. While the impact of the Postal Civil Service Retirement System Funding Reform Act of 2003 reduced benefit costs to $13.3 billion in 2003, we expect benefit costs to re-escalate beginning in 2004, rising to $20.8 billion in 2010.

During the past 20 years, postal benefits have grown at an average annual rate of 5.5 percent. This compares to the private sector annual growth rate of 4.4 percent.

The solution to this issue is managing benefit costs, ideally by bringing them within the purview of collective bargaining or by adjusting them through statute. It is not our intention to reduce the benefits already enjoyed by current and retired Postal Service employees. Benefit negotiations would affect only eligible employees entering the Postal Service following the conclusion of negotiations.

Workers' compensation represents a sizeable portion of our compensation and benefit costs. In fiscal year 2003, $1.5 billion in workers' compensation costs accounted for 2.9 percent of our total $50.5 billion in compensation and benefit costs. At the end of 2003, total liability for future workers' compensation costs was $7.1 billion. In 2003, an additional $704 million was paid in compensation and benefit costs for employees with work-related injuries in either limited duty or rehabilitation positions. We are also responsible for $122 million in workers' compensation costs incurred by the Post Office Department prior to 1971.

The best way to limit workers' compensation costs is through a strong safety program that helps to reduce the number of work-related injuries and illnesses. Our program is doing that. From 2001 through 2003, workplace injuries were reduced by an impressive 28 percent. But workers' compensation expenses, which were $970 million in 2001, grew by more than 50 percent, to $1.5 billion in 2003.

The magnitude of workers' compensation costs has been a concern since the early days of postal reorganization. Although these costs were moderate in the years immediately following reorganization, they grew significantly with the 1974 amendments to the Federal Employees Compensation Act. Among other changes, these amendments eliminated the reduction in the level of workers' compensation benefits at age 70 and eliminated the immediate, three-day waiting period before benefits could be paid. The waiting period was moved from the date of injury to three days after the end of the 45-day period of continuation of pay received from the Postal Service by an injured employee.

The President's Commission has recommended statutory changes affecting workers' compensation in the Postal Service. We support these recommendations, which can significantly reduce costs, and urge their adoption.

One recommendation is that postal employees on workers' compensation rolls have their compensation reduced at some point to reflect the fact that they would likely have retired were they not on the rolls of the Office of Workers' Compensation Programs. A recent review by the Office of Inspector General found that 2,819 – or 21 percent – of the more than 13,000 Postal Service employees on workers' compensation are classified as totally disabled and, as a result, not expected to return to work. Of that group, almost 90 percent – 2,502 – are age 55 or older and likely to be, for the most part, retirement-eligible.

Our own analysis shows that for two similarly situated retirement-eligible employees, one who selects optional retirement and the other who continues on the OWCP rolls, there is a disturbing disparity. Over a ten-year-period, the employee who continues receiving workers' compensation receives $95,000 more than the employee who retires.

Another of the Commission's recommendations regarding workers' compensation involves reinstating the three-day waiting period before an employee is eligible to receive 45-days continuation of regular pay rather than after the 45-day period. This is consistent with individual state workers' compensation programs that require a three- to seven-day waiting period before benefits are paid. An appropriate waiting period in the Postal Service should exist at the beginning of the coverage period, as is the case in the private sector.

In the area of employee health benefits, we expect annual costs to increase, on average, $418 million through 2010. Implementing private sector practices in connection with plan design and efficiency could provide the opportunity to improve the delivery of benefits and reduce costs. This would require mandatory bargaining of this benefit with our unions.

Retiree health benefits are now defined by federal law. We project annual cost increases of more than 16 percent – some $228 million annually – for this benefit through 2010. We believe that changes are possible that address cost concerns as well as issues of fairness. Today, benefit levels are the same for an employee who has worked for five years or for thirty-five years.

We expect cumulative costs for all benefit categories to rise by about $1 billion per year over the next six years. Clearly, there are opportunities to control the unrestrained growth of these costs while, at the same time, protecting the legitimate interests of Postal Service employees. I urge that you consider these approaches as an integral part of any comprehensive reform legislation.

Any discussion of Postal Service costs – particularly those over which we have limited control – must inevitably lead to a discussion of postage rates and possible price caps. Price caps have been at the center of the various reform bills that have been offered over the last several years in connection with the Postal Service's call for pricing flexibility – a flexibility that could provide sought-after predictability for mailers.

At their best, price caps would accurately be set against the reality of postal costs and revenues within a given time period. Yet, as we have learned since 2001, the volatility of today's mail market has defied projections. Just four years ago, the Postal Service's *Five Year Strategic Plan, 2001-2005* projected a mail volume of 230 billion pieces for fiscal year 2004. Even with the Plan's "rapid diversion" scenario, the Plan projected mail volume of 213 billion pieces in 2004. This year, our projections call for no significant change from 2003 volume of 202 billion pieces. As volume falls, particularly for First-Class Mail, revenue obviously declines, as well.

An appropriately constructed price cap will allow the Postal Service to recover costs over which it has little or no control. As I have explained, there are significant cost drivers beyond our control. The Postal Service is particularly vulnerable to increasing fuel costs, given our need to transport mail to and from 38,000 facilities and to more than 141 million addresses six days a week. Other delivery and trucking firms, including FedEx and UPS, routinely impose fuel surcharges to deal with increasing costs. In addition, our network must grow each year to accommodate average annual growth of more than 1.8 million new addresses. In terms of inflationary pressure, the statutorily mandated benefits costs for employees and retirees, including health benefits, workers' compensation and annuities, are of even greater concern. We believe the Postal Service should be able to bargain over these benefits. If we do not receive that flexibility, then these costs must be recognized in the pricing scheme.

Finally, the price cap must take into account a cost for which the Postal Service and its unions bear full responsibility: wage increases. The Postal Service, due to the very nature of the service it performs, is far more labor-intensive than most other employers. The Postal Service believes that the Employment Cost Index (ECI) wage series, the broad measure of wage gains in the economy as a whole, represents an appropriate metric for this component of our costs.

Each of these factors must be considered in the construction of a price cap. While a number of models have been discussed, using a variety of indexes, it is clear that Postal Service costs are, in many ways, different from those of other industries and businesses. Therefore, the success of a price cap is entirely dependent on its ability to accurately project and reflect postal costs during the covered period. We believe the appropriate price cap, therefore, would be made up of at least four components: a fuel index, a network expansion index, the actual growth in statutory benefits, and ECI wages. There may be other factors that should be taken into account, as well.

This price cap does not envision a continuation of the present "cost of service" price regime. It will take aggressive management by the Postal Service to successfully operate at or below the cap. The reason is simple. Unlike other regulated networks, the Postal Service imposes no separate charge for delivery. The Postal Service must generate sufficient revenues to simply maintain a network – our 347,000 letter carriers and our 38,000 retail outlets.

First Class Mail, the Postal Service's flagship product, contributes about $17 billion toward coverage of this expense. Yet, First Class Mail volumes have declined the last three years. In Fiscal Year 2003 alone, this decline represented a loss of $642 million in contribution to network costs. The need to recoup this loss of contribution would, in and of itself, cause an added increase in the rates sought by the Postal Service in the next case it files under current law. However, under the price cap I have described, the Postal Service, if it were to operate successfully under the cap, would have to offset lost contribution with productivity gains.

Given the very real volatility in today's mail market, my very real concern is that an imperfectly crafted price cap would be unworkable. That could require the Postal Service to file an exigent rate case as the rule rather than the exception. If that were to occur, it would defeat the purpose of a price cap and, in raising rates beyond those defined by the cap, contribute to even greater mail volume decline, leading to a vicious spiral of destructive rate increases.

For this reason, should price caps be a part of postal reform legislation, I urge you to consider, thoroughly and carefully, the construction of a price cap regime that drives maximum operational efficiency but does not undermine the legitimate financial needs of the organization and the level of service provided. Should you leave the determination of the appropriate pricing scheme to the regulator, we believe Congress must provide adequate guidance to ensure the regulator considers these important factors.

This price-cap regime could eliminate a cumbersome rate-setting process and result in smaller, annual increments that can be absorbed by our commercial customers. At the same time, we strongly believe that marketplace uncertainties mandate that a price cap be just one element of comprehensive reform legislation that provides the Postal Service with flexibility in other critical areas.

Like each of you, the Governors of the Postal Service and its senior management have devoted a great deal of time to the consideration of the many different elements that would be part of a successful legislative reform initiative. Just a few short years ago, we could not have predicted that the President would have established a Commission to examine the problems facing the postal system and recommend solutions. Just a few short years ago, we could not have envisioned that the Senate and the House of Representatives would hold a joint hearing as the culmination of months of independent hearings on this subject. And just a few short years ago, we could not have imagined that First-Class Mail volume had reached its peak and would begin what appears to be an inevitable and, possibly, permanent decline.

Looking ahead just a few short years, it is likely that today's projections, today's assumptions and today's analyses may be just as obsolete as those of just a few short years ago. The legislative approaches we have considered may have been sufficient had the dynamics of the mail market conformed to our expectations. They have not.

The solutions we are considering today may provide financial stability for a limited period. But electronic diversion will continue to occur – and at a more rapid rate than we are experiencing today. Even the most carefully constructed price cap will result in rate increases that will accelerate the decline in overall mail volume. If we do not significantly restrain costs that are not under our control, we threaten the affordability of the mail, further eroding volume and revenue.

If we are to succeed in this effort, we must expand our thinking. We must reconsider the definition of universal service as we know it today. Can we continue to afford six-day mail delivery, at a single price, to virtually every home and business in America? As we prepare for the future, our deliberations must include this critical issue. And, depending on how we answer this question, we must consider who will make this decision and how it will be implemented.

It is not my intention to reduce mail delivery from six days to five. I have previously stated that this will not happen on my watch. I have not changed my position. But, as Postmaster General, it is my obligation to bring this issue, which could be central to the ultimate success of our reform efforts, to the conversation.

Finally, I want to comment on two issues raised at an earlier hearing by our competitors. The first concerns the postal monopoly. In his testimony, Fred Smith, CEO of FedEx, made the claim that "the postal monopoly is rendering the Postal Service unfit to compete and prosper in the delivery services sector of the future." His proposition rests on the notion that by creating a "protected market," the Private Express Statutes make it virtually impossible for the Postal Service to be efficient.

That is simply not the case, as our record of service performance and cost reductions clearly indicates.

The worksharing partnerships we have formed with mailers over the past 25 years also attest to the efficiencies gained by mailers who perform the work of preparing their mail for automated processing and delivery by the Postal Service.

And Michael Eskew, Chairman and CEO of UPS, in his statement to the Committee on Governmental Affairs earlier this month, said, "The Postal Service's mail monopoly allows it to subsidize competitive products and inappropriately compete with the private sector."

That statement misses the mark on both counts. First, the Postal Service's monopoly on letter mail does not subsidize competitive products. In fact, as First-Class Mail volume continues to decline, so too does its contribution to system costs. I would point out, too, that in 2003, our competitive products, Express Mail, Priority Mail and Package Services contributed $2.5 billion to system costs.

But there is an even bigger misconception in Mr. Eskew's statement. The Postal Service is prohibited by law from cross-subsidization. Period. And one of the duties of the independent Postal Rate Commission is to ensure that this does not occur.

The reference to "inappropriate competition" with the private sector ignores an important lesson of history. At the turn of the 20th century, by law, the Post Office Department was not permitted to carry parcels weighing more than four pounds. Only private express companies delivered larger packages.

Back then, more than half of the American public lived in rural areas, many of whom received no parcel delivery from private carriers and, for some who did, only at extremely high rates.

When the Parcel Post Act of 1912 was enacted, all that changed. It was an instant success. Three hundred million parcels were mailed in the first six months the service was offered. The new Parcel Post service launched a multi-billion-dollar mail-order catalog business in America. For the first time in history, rural residents were able to use the mail to receive the goods they needed at affordable rates. Even today, almost a century later, that holds true, as the Postal Service delivers to every address – city or country – without a residential or rural surcharge. This remains at the heart of today's promise of universal service.

Through the efforts of so many in Congress, the Administration and the mailing industry, we have reached a point of virtually unanimous agreement about the need for postal legislative reform. I believe we are closer today to achieving this goal than we have ever been.

I believe that, working together, it is possible to achieve proper balance between increased flexibility for the Postal Service and an effective level of independent oversight. In achieving that balance, we have the opportunity to create a legacy of customer-responsive service that serves everyone in our nation equally – and equally well.

As Postmaster General, I do not seek change for the sake of the Postal Service. Rather, as their common agent, the Postal Service seeks change for the sake of every individual, every family and every business that relies on the mail.

Yes, there are challenges connected with the next steps, but the rewards for the people of our nation cannot be understated. If we are successful in our efforts, we will preserve the right of every American to affordable, universal mail service. That is what we provide today. That is what we want to be able to provide for many years to come.

Again, I would like to take this opportunity to offer my gratitude to Chairman Collins and Chairman Davis for holding today's joint hearing and the many hearings that preceded it. It is clear that there is a real interest among the members of both Committees in creating a new business model that will protect this basic public service for many generations to come. I look forward to working enthusiastically and cooperatively with you in pursuit of our common goal.

Thank you. I will be happy to answer any questions you may have.

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